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JOHN T. FEY,

IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 524

AUTOMATIC CIGARETTE SALES CORPORATION
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Printed by Action Printing Co., 518 Fifth St., N. W.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioner, Automatic Cigarette Sales Corporation, by its attorney, Thurman Hill, prays that a Writ of Certiorari, be issued to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in the above entitled case on June 5th, 1956.

OPINIONS BELOW

The opinion of the Tax Court of the United States is reported in 14TCM No. 15, 1955, Dec. 20, 829 (M). The opinion of the Court of Appeals for the Fourth Circuit is reported in 234 F. 2d, 835.

JURISDICTION

The jurisdiction of this Court is invoked under Title 28 U.S. Code, Sec. 1254 (1). Jurisdiction of the United States Court of Appeals for the Fourth Circuit was based on Section 1141 (a) Internal Revenue Code, as amended, and that tax returns for the years involved were filed with the Collector of Internal Revenue for the District of West Virginia, located at Parkersburg, West Virginia, the office of which Collector is within the jurisdiction of the United States Court of Appeals for the Fourth Circuit. By order of Mr. Justice Black, dated August 21, 1956, the time of petitioner for filing for Writ of Certiorari was extended to and including October 26, 1956.

QUESTION PRESENTED

Whether the mere physical possession for a temporary period by petitioner, as custodian, agent or trustee, of monies belonging to others for payment to a third party can meet the definition of "income" so as to require the reporting thereof in petitioner's income tax return and the payment of taxes thereon?

STATUTE AND DEFINITIONS INVOLVED

Internal Revenue Code: Sec. 61. Gross Income Defined. (Sec. 61 (a) 1.

(a) GENERAL DEFINITION.—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

(2) Gross income derived from business;

(3) Gains derived from dealings in property;

(4) Interest;

(5) Rents;

(6) Royalties;

(7) Dividends;

(8) Alimony and separate maintenance payments;

(9) Annuities;

(10) Income from life insurance and endowment contracts;

(11) Pensions;

(12) Income from discharge of indebtedness;

(13) Distributive share of partnership gross income;

(14) Income in respect of a decedent; and

(15) Income from an interest in an estate or trust.

Funk and Wagnalls' New Standard Dictionary of the English language:

"Income—The amount of money coming to a person or corporation within a specified time or regularly (when unqualified annually), whether as payment for services, interest, or profit from investment; revenue."

Black's Law Dictionary:

"Income—The return in money from one's business, labor, or capital invested; gains, profit, or private revenue."

Webster's New Collegiate Dictionary:

"Income—1. A coming in; specif., beginning; advent. 2. Something that comes in as addition. 3. That gain or recurrent benefit (usually measured in money) which proceeds from labor, business, or property; revenue; receipts.

Constitutional Construction and Interpretation:—The Federalist.

VI. Construction of Words and Phrases.

1. Common and Ordinary Meaning.

"No word or clause can be rejected as superfluous or

unmeaning, but each must be given its due force and appropriate meaning. Words in a constitution, as well as words in a statute, are always to be *given the meaning they have in common use* unless there are other strong reasons to the contrary. They are to be taken in their natural and obvious sense, and *not* in a sense unreasonably restricted *or enlarged.* Words and terms are to be taken in the sense in which they were used and understood at common law and at the time the Constitution and the amendments were adopted. They were used in their normal or ordinary, as distinguished from their technical meaning. Where any particular word or sentence is obscure or of doubtful meaning, taken by itself, its obscurity may be removed by comparing it with the words and sentences with which it stands connected." (Emphasis supplied)

STATEMENT

The controversy involves the proper determination of the petitioner's liability for Federal income taxes, declared value excess profits taxes, and excess profits taxes for the calendar years 1944 and 1945 in the controverted amount of $125,046.47. More especially does it concern the inclusion in the petitioner's income of the sum of $73,246. belonging to third parties. This petition will concern itself with that facet of the overall problem.

The petitioner, during the calendar years above-named, 1944 and 1945, and for some years theretofore, was engaged in the business of buying, selling and leasing coin and vending machines, including cigarette, juke, (music) box, and game and slot machines, and other similarly operated coin machines. The petitioner itself, was not engaged, however, in the business of operating any of said machines, but leased them to other individuals or corporations who did the actual operating of same. It was the custom of the City of Wheeling, West Virginia, in determining revenues needed for the operation of the city, to include therein fines which would be obtained from those indi-

viduals or corporations who operated slot machines within the city's jurisdiction. This custom, in fact and in effect, ignored the ordinance prohibiting the operation of gambling devices and substituted therefor the regulation of such operation by a system of fines. This custom and policy existed during the years 1941 through 1946. This procedure or custom was so exact that a specific levy against the operator was attached to each machine in the amount of $106.00 per location, which sum was composed of $100.00 fine and $6.00 court costs. These sums were paid to the Judge of the City Police Court and entered upon the official records of the Court in the name of the *location owner* who had leased the machines from Automatic. *The fine was never levied against the petitioner or paid by it with its own monies.* At various intervals, a representative of the Petitioner would collect the monies from each machine and divide the amount thereof equally between the location owner and Automatic. Out of the half of such collection belonging to the location owner there would be deducted an amount sufficient to satisfy the fine and court costs of $106.00 per machine per location. Such sums of $106.00 per machine per location never became the property of, or income to, the petitioner. By custom and practice, the latter acted solely in the capacity of an agent, or as a custodian through which monies belonging to the location owner, representing fines and court costs, were channelled or conveyed to the municipal government. It must always be borne in mind that the city never proceeded against, but by custom and practice, waived, the petitioner's type of activity, the ordinance being interpreted solely against the operation of the machines, not their possession or leasing. As the monies representing the fines and court costs were in the hands of Automatic solely as custodian, trustee, or agent, it could never be construed as income to Automatic. Notwithstanding this readily apparent picture of the transactions, the Commissioner ruled such fines and court costs of third parties (paid out of monies

belonging to them) to be income to Automatic and assessed deficiencies thereon. As a result thereof, the Commissioner included in the income of the petitioner an additional amount of $73,246.00 belonging to third parties, representing fines and court costs collected by Automatic for the City of Wheeling, West Virginia. It is also a fact that said $73,246.00 was turned over by petitioner to the City of Wheeling, West Virginia.

The Tax Court of the United States and the Court of Appeals for the Fourth Circuit both found that the monies for the payment of the fines were deducted from the 50% share of the location owners, not from the petitioner's 50% share and was in fact turned over to the City of Wheeling, West Virginia without diminution. Notwithstanding such finding, said sum of money was held by the Tax Court and Court of Appeals to be includable in petitioner's income upon which a tax would have to be paid. These decisions were in direct opposition to the findings of both courts and, accordingly, wholly inconsistent therewith.

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals erred:

(1) In improperly and wrongfully drawing a conclusion not supported by, but in violence of, its own finding of fact; namely, that monies belonging to a third party and in a tax payer's hands purely and solely as custodian, agent or trustee, are subject to inclusion in said tax payer's gross income, thus rendering him liable for taxes thereon.

(2) In wrongfully and immorally distorting and enlarging (a) the classic definition of income handed down by the Supreme Court of the United States' decision in *Eisner* v. *Macomber*, 252 U.S. 189, 40 S. Ct. 189; (b) The definition of gross income as set forth in the Internal Revenue Code, Sectior 61 thereof, and, (c) The common, ordinary and accepted definition of the word in the English language.

(3) In failing to follow its own finding of fact that $73,246. represented the total of monies belonging to third parties and by petitioner turned over to the City of Wheeling, West Virginia and conclusively thereby not includable in petitioner's taxable income.

(4) In affirming the decision of the Tax Court of the United States as it pertains to the taxability of said sum of $73,246. to petitioner.

REASONS FOR GRANTING THE WRIT

The decision in this case will effect a substantial segment of the Nation's business; i.e., individuals and corporations serving as trustees, custodians or agents. To impose the possibility of personal liability upon those acting in such fiduciary capacities, merely on the whim of a tax collector backed up by *a court that failed to follow its own findings,* would be a deterrent so effective as to negate the further use of the fiduciary relationship. Further, to sustain the decision would be to give approbation to a lower court which felt itself not bound by (a) a decision of this Court, (b) by the Constitution, or (c) *its own finding.* With this decision an accomplished fact, albeit anomalous, we are reminded that the Law is not above reason, the Law is reason intelligently applied. A court that concludes opposite to its own findings does not meet that mandate and especially so where the conclusion violates the Constitution and direction of a higher court.

The instant decision involves these important questions of law which have not been, but should be, settled by this Court. Among other things, it queries whether a decision of this Court has binding effect upon the lower courts or whether such lower courts can with impunity, and without fear of reversal, enlarge the scope of past decisions and rulings of the Supreme Court of the United States. It also queries whether a Court, by its decision, can do what even Congress can't; namely, adopt a definition contrary to the Constitutional use (common speech) which in effect

would be an alteration of that document. For this latter purpose there is only required a clear definition of the term as used in common speech. (see p. 3)

There is a clear conflict, by enlargement and distortion, between the ruling of the Court in the instant case and the decision of this Court in *Eisner* v. *Macomber,* 252 US 189, 40 Sup. Ct. 189. Again, it is in clear conflict with the ordinary meaning of the term "income" as used in the Constitution and the tests therefor set out in Section 61 of the Internal Revenue Code. In the *Eisner* v. *Macomber* case (supra) the Court adopted and reaffirmed the Constitutional meaning as

> "Income may be defined as the gain derived from capital, from labor, or from both combined."

More specifically, the Court went on to point out those things which may be considered income and which, if not therein included, would fail to answer that designation. Mr. Justice Pitney, in pointing this out, stated income to be

> "A gain, a profit, something of exchangeable value, *proceeding from* the property, *severed from* the capital, however invested or employed, and *coming in,* being "derived"—that is, *received* or *drawn by* the recipient (the tax payer) for his *separate use,* benefit and disposal—*That* is income derived from property. *Nothing else answers the description.*" (Only last emphasis supplied).

With that definition in mind, how can it be said that the sums totaling $73,246. could ever be for the *separate* use, benefit and disposal of the petitioner? Such funds were received by petitioner from the location owners and by it turned over, intact, to the City of Wheeling. Certainly such funds cannot meet the description given by Mr. Justice Pitney and his admonition, of failure to answer the description, renders such sums not income to the petitioner. It is patently clear that payment of the fines benefited the location owners so on that ground too it does

not meet the "separate use, benefit and disposal" required by Mr. Justice Pitney.

In this same learned discussion it was pointed out that not even Congress could adopt a definition of a word which would in effect alter the Constitutional meaning, which latter derived from common speech. (P. 3-4 hereof) Using common speech as a norm for our guidance would be in complete harmony with the form and style of the Constitution and its conciseness and lucidity. As stated heretofore, the lower court did not confine itself to the Constitutional or common speech, meaning of the word "income" as "gain derived from capital, from labor or from both combined", but added a further classification to include monies held by one party belonging to another party for transmittal to a third party. Nowhere in the lower court's finding is the sum of $73,246. designated as a gain to the petitioner derived from capital, from labor or from both combined. Actually, the lower court, in specific terminology, found that the total represented sums belonging to third parties turned over to petitioner for the purpose of paying fines to be assessed against the owners of the money. This will be pointed out more fully in petitioners concluding contention.

Now to that concluding contention. In the lower court's decision, P. 2, it finds

> "The record shows that in 1944 the tax payer installed a large number of gambling slot machines in various locations in the City of Wheeling and *divided the proceeds of the operations between itself and the proprietors of the stores where the machines were placed.*" (Emphasis supplied).

It is true that these operations were in violation of State and Municipal prohibitions but it is also true and factual that as interpreted and enforced by the City Fathers, action was taken solely against the operation of the machines, not against their possession or rental. This technique applied not only to petitioner but to all others similarly engaged.

However, what petitioner desires to point out is that the Court found the proceeds were divided between the store owners and the petitioner. That being so, any conclusion of the Court, to be proper, would have to have foundation in that finding.

Again, the Court found, in Pages 2-3 of its opinion, that

> "The testimony of most of the location proprietors who appeared as witnesses, however, showed that the money was first divided equally between the proprietor and the collector, but *then the amount of the fine was deducted from the proprietors' share* and retained by the collector." (Underscoring supplied).

With that specific finding staring the petitioner in the face it becomes purely involuntary for petitioner to explode and demand in the vernacular, "*How can something that belongs to somebody else be taxable to someone that it doesn't belong to?*" The instant and second the division was made, 50% of the money in the machine belonged to the location owner. That was his with full and complete title. Subsequently, no matter how soon thereafter, a portion of that money belonging to the location owner was given to, and retained by, petitioner's Collector, *NOT* for the use and benefit of petitioner, but to pay a fine which the location owner *knew* would be assessed against him and for which he was liable. In other words, it would be paid to the City for the benefit of the location owner (in satisfaction of the location owner's fine). No mental gymnastics can change a fact, and no court properly may infer or conclude anything opposite to the *fact itself*, especially if such inference or conclusion results in a denial of the existence of the fact as here. Nonetheless, the lower court has so done in our case. The mere fact that petitioner might have been engaged in an improper and illegal transaction with the City Fathers does not change one iota that the Court found the sum of $73,246. was deducted from the proprietors' share. It is purest fantasy to attempt to argue that

when petitioner temporarily held monies that came from the proprietors and were transmitted by petitioner to the City of Wheeling that such temporary possession rendered it liable for taxes thereon as income. This is apparently nothing but a barefaced attempt improperly to enhance the collection of the revenues at petitioner's expense.

For a moment, let us be as illogical as was the court's conclusion. For that purpose, let us assume that the fines and court costs were set up by the City in the name of and paid by the petitioner from his share pursuant to arrangement between the City and location owners. Now, let us also assume that the tax collector discovered this situation; would he, as he has done herein, hold the total of the fines paid to be income to the various location owners? The mere recital of such a fantastic improbability is its own answer. It was not petitioner's money that was taxed. The Court itself said it was location owners' money retained by a collector of petitioner.

It is of much persuasive import to point out that even the respondent does not deny that petitioner's failure to turn over such sums to the City Fathers would have rendered it liable, civilly and criminally, for embezzlement. It is axiomatic that the withholding of such funds as would lead to a successful prosecution for embezzlement never, under any circumstances, vests property thereto in the withholder.

While it is not mandatory on the Court of Appeals to accept a decision of a lower court, if that decision is however arrived at by the use of reason intelligently applied it can be of persuasive import to this Court. That is especially true where it concerns facts and circumstances similar to those present in the instant case. The only difference in the case to be cited was that instead of the location owners paying the full amount of their fines it was agreed between the owner of the machines and such location owners that it would be split 50-50. Speaking for the Tax

Court in *Charles A. Clark v. Commissioner*, 19 TC 9, Judge Van Fossen ruled

> "The payments of $12.50 per machine per month made by the proprietors of the other locations through petitioner, *as a conduit*, should not be included in his income. *Petitioner derived no benefit* from such payments. * * * The arrangement by which petitioner made the payments was *merely one of convenience.*" (Emphasis supplied.)

It is a fact, in our case, that the lower court found the full sum of $73,246., received by petitioner's collector from the location owners, was remitted without diminution to the City of Wheeling.

The lower court having made its finding and arrived at a conclusion ill-mated therewith, attempts to rescue the illegitimate offspring by conceiving that the location owners were all part of one big business family fathered by the petitioner. (Page 4, Court's Opinion).

That "conception" is still-born as nowhere in the record, in the evidence produced or in the court's own findings, is it apparent. It is purely gratuitous and worth what it cost. The individual location owners were separate and apart and therefore independent of petitioner. They owned their own premises, or rented them from third parties, and were subject to no control or direction from petitioner. They exercised their own judgment, opened their establishments when they desired, closed them at whatever hours they liked, hired such employees as they required, all without regard to any approval, disapproval or other suggestion from the petitioner. All of these location owners individually owned and operated various and separate types of establishments such as cigarette and cigar stores, bar-rooms, poolrooms, bowling alleys, etc., none of which, in any manner of fashion, were subject to petitioner's direction or control. They could have the rented machines taken out whenever they decided, refuse permission for their operation, and in all matters and manner act freely without any control what-

soever from petitioner. The location owner was in letter and spirit, in fact and in substance, a true entrepreneur, a rugged individualist.

Are these the indicia of a one-unit enterprise belonging to petitioner or rather are they indicia of what in fact they were, completely separate, distinct and individual units free from any control, direction, or domination from petitioner or from each other.

If the Government or the lower court seriously contends all of this was "a business which belonged" to the petitioner, how come it was not included in the petitioner's operating receivership, theretofore and now active in the Federal Court at the respondent's demands? That it was not conclusively shows the lower court was reaching for a straw and didn't take even itself seriously.

Further, and solely to show the confused state of mind present in the lower court when its opinion was drafted, it cited *Commissioner* v. *Charles V. Doyle,* CA 7, 4/11/56, as sustaining a certain proposition when in fact it is in opposition thereto. (Opinion, Page 4).

As this forum is the last for petitioner it respectfully prays that this Court grant the writ so as to make an end to injustice, rather than injustice without end. If the decision of the lower court proves anything it is only, that court's being composed of human beings, have the inherent fallacies of homo sapiens. They are swayed by the same emotions that affect the man in the street. The majority stock holder of petitioner, William Lias, has been given, justly or unjustly, a malodorous reputation. Having given the "dog a bad name" it sticks, seemingly, forever after no matter how just, fair and equitable may the later cause be. There was absolutely no necessity for the lower court to mention the past criminal case concerning the majority stockholder of petitioner. It had absolutely no legal significance, purely emotional. Unfortunately, while emotions are pleasant they oft blind the eyes of Justice and render unjust decisions. Using the same analogy and metaphor

the petitioner prays that instead of the "give the dog a bad name" concept that this Court let "the dog have his day".

To summarize the basic reasons why a writ should be issued herein, the petitioner states:

1. The decision of the lower court herein conflicts with the Supreme Court of the United States in *Eisner* v. *Macomber* (supra) in that it enlarges improperly and without basis in Law or in fact the definition of "income".
2. The decision of the lower court conflicts with the Constitutional use, and the common speech meaning, of the word "income".
3. The lower court's decision is in complete conflict, an enlargement and distortion, of the term "income" as set forth in Section 61 of the Internal Revenue Code.
4. The lower court's decision is improper and unsound in that the conclusion is not predicated on the court's own finding but in direct and complete opposition thereto.
5. The lower court's decision herein is on the important question of what constitutes "income" under the Internal Revenue laws and vitally affects the fiduciary relationship of individuals and firms acting as agents, custodians, or trustees.

CONCLUSION

For the foregoing reasons, the petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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Receipt is hereby acknowledged of a copy of the within this day of October, 1956.

Attorney General

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

Filed June 5, 1956. R. M. F. Williams, Jr., Clerk.

No. 7152.

AUTOMATIC CIGARETTE SALES CORPORATION, *Petitioner,*
versus
COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

On Petition to Review the Decision of The Tax Court of the United States.

(Argued April 18, 1956. Decided June 5, 1956.)

Before PARKER, Chief Judge, and SOPER and DOBIE, Circuit Judges.

Thurman Hill (Arthur J. Swanick on brief) for Petitioner, and Homer R. Miller, Attorney, Department of Justice (Charles K. Rice, Assistant Attorney General; Lee A. Jackson and A. F. Prescott, Attorneys, Department of Justice, on brief), for Respondent.

SOPER, Circuit Judge:

This case involves deficiencies in income, declared value excess profits and excess profit taxes for the year 1944, in the sum of $132,725.14. The principal questions for decision concern (1) the inclusion in the taxpayer's income of the

sum of $73,246.00 paid by the taxpayer in fines for the illegal operation of slot machines in Wheeling, West Virginia and (2) the amount allowed by the Commissioner of Internal Revenue for depreciation on taxpayer's slot, music and cigarette machines.

Automatic Cigarette Sales Corporation was engaged in the business of buying, selling and operating cigarette, juke box, game, slot and other machines. The corporation was controlled by William G. Lias, its president and principal owner, who was tried and acquitted on the charge of income tax evasion in the District Court of the Northern District of West Virginia in June, 1949. Some of the evidence given at the trial of the criminal case was received by the Tax Court in the pending case under a stipulation of the parties. The record shows that in 1944 the taxpayer installed a large number of gambling slot machines in various locations in the city of Wheeling and divided the proceeds of the operations between itself and the proprietors of the stores where the machines were placed. These operations were in violation of §6094(1) of the West Virginia Code of 1949 and of §32 of Ordinance 38 of the City of Wheeling. The use of the machines, however, was permitted under an arrangement between Lias and the city authorities whereby fines of $100.00 and costs were imposed periodically upon the operation of each machine after a check by the city police department. When the check was complete the chief of police notified the taxpayer of the number of machines and the names and addresses of the location proprietors. The list was then handed to the judge of the police court, who imposed fines and costs in the names of the location proprietors and made an official record thereof. The taxpayer's name did not appear on these lists. The location proprietors, however, were never served with warrants and were never brought into court. The city looked to the taxpayer for the payment of fines and the taxpayer actually paid them. The only information which the location proprietors had

as to the imposition of the fines was that the taxpayer's collectors deducted the amount of the fines from the monies taken from the machines. There was some variation in the testimony as to the procedure for the division of these monies. The testimony of most of the location proprietors who appeared as witnesses, however, showed that the money was first divided equally between the proprietor and the collector, but then the amount of the fine was deducted from the proprietor's share and retained by the collector.

Taking this testimony in connection with the records of the police court, which indicated that the fines were levied against the location owners and not against the taxpayer, the contention is made on its behalf that the monies used to pay the fines did not constitute income of the taxpayer but merely passed through its hands as the agent of the proprietors against whom the charges were filed. The taxpayer relies in this connection on *Clark* v. *Commissioner*, 19 T.C. 48, where the court held in a slot machine case that monies taken from the machines by the owner and used in the payment of fines imposed upon the owner and the location proprietor jointly should be treated to the extent of one-half as the income of the owner and one-half as the income of the proprietor. The court found that the latter one-half merely passed through the taxpayer's hands as a conduit and that he derived no benefit therefrom.

Without expressing any opinion as to the correctness of this decision, we are satisfied that the Tax Court was justified in refusing to follow it as a precedent in the pending case. The evidence clearly warrants the finding that the taxpayer was not only the owner of the machines but also the operator and manager of the business through its president and principal owner to whom the city looked for payment of the fines which had been agreed upon. Certainly the shopkeepers as well as the corporation were guilty of violating the law and were subject to the payment of the fines; but the Tax Court was not obliged to accept the police

records as a correct statement of the legal position of the parties in what was evidently an irregular and illegal transaction. Hence the payment of part of the proceeds of the business to the local proprietors for the use of their premises and the listing of the charges in the police court in their names may fairly be regarded as incidents of a business which belonged to the corporation. In this view, the money used in the payment of the fines was part of the taxpayer's income but it was not deductible as an ordinary and necessary business expense under §23 of the Internal Revenue Code because it was incurred in the violation of a State statute and a city ordinance and a tax deduction would frustrate the sharply defined policy of the commonwealth. *Commissioner* v. *Heininger,* 320 U.S. 467; *Lilly* v. *Commissioner,* 343 U.S. 90; *Commissioner* v. *Charles V. Doyle,* CA 7, 4/11/56.

The question of depreciation turns on a finding of fact as to the length of the useful life of the taxpayer's machines. The taxpayer rests its case in this regard, for the most part, on the testimony of an expert witness, while the Commissioner depends upon the presumption of correctness which attends his determinations, the practice of the taxpayer in regard to depreciation in prior years, and the failure of the taxpayer to produce any witness with actual knowledge of the machines in question.

Prior to 1940, before the enactment of the excess profits tax law, the taxpayer calculated depreciation of its slot machines on the basis of a 3-year life for new and a 2-year life for used machines, and depreciation of its cigarette and music machines on the basis of 5 years for new and 3 years for used machines. After 1940 the taxpayer made no distinction between new and used machines and attributed a life of 1 year to slot machines and a life of 4 years to cigarette and music machines.

For the year 1944 the taxpayer claimed depreciation in the amount of $38,700.87 for slot machines, $11,672.41 for

music machines, and $1,084.30 for cigarette machines, and having sold a large part of the machines in that year, reported a capital gain on the reduced cost basis of $101,788.86. The Commissioner adjusted the depreciation rates to correspond to those used by the taxpayer prior to 1940 and made a determination which reduced the taxpayer's capital gains to $74,582.09 but increased the taxable income from the taxpayer so as to create the tax deficiencies under consideration.

The taxpayer relies for its rate of depreciation on the testimony of a machine repairman who entered its employ in 1937 at the age of 18, served in the army from 1942 to 1946 and returned to the taxpayer at the end of his military service. He had no actual knowledge of conditions in the business between 1942 and 1944. He testified that the mechanical machines had a possible life of 18 months, a longer period than that claimed by the taxpayer, and that the music and cigarette machines had a possible life of 5 years, the period used by the taxpayer prior to 1940 and adopted by the Commissioner in this case. Hence his testimony supported the claim of the taxpayer only in respect to electrical machines and did not support its claim with respect to gambling slot machines or the music and cigarette machines. Moreover, his testimony showed that the taxpayer kept service and shop machine records, and these were not produced at the hearing.

We think that the Tax Court was entirely justified in holding that this testimony was insufficient to sustain the taxpayer's contention. Taken at its face value it failed in important particulars to support the taxpayer's calculations and it was not corroborated by evidence of the actual length of life of the machines, either from the taxpayer's records or the testimony of persons who had personal experience in handling the articles. There are cases in which it has been held that the rejection of uncontradicted testimony of the Tax Court constitutes reversible error, see

Wright-Bernet v. *Commissioner*, 6 Cir., 172 F. 2d 343; *Mayson Mfg. Co.* v. *Commissioner*, 6 Cir., 178 F. 2d 115; but it is the duty of the Tax Court to weigh expert as well as factual evidence and to reject it when there is reason to believe that it is unreliable. See *Dayton P. & L. Co.* v. *Commissioner*, 292 U.S. 290, 299; *Miles-Conley Co.* v. *Commissioner*, 4 Cir., 173 F. 2d 958. We think that the Tax Court exercised this authority in a proper manner in the pending case.

In addition to the arguments on the merits, the taxpayer now contends that the Tax Court denied it due process by refusing motions filed on its behalf to vacate and reconsider the court's adverse decision and to allow it to produce additional testimony bearing on the controversial issues. The motion for reconsideration contained an offer to produce William G. Lias as a witness to the transactions involved and as an expert with regard to the useful life of the machines; and also an offer to produce one Jacob Dobkin, a competitor of Lias in a similar business in the city of Wheeling, as an expert on the same subject. The failure to produce Lias at the hearing was explained on the ground that he was unable to attend because he was mentally and physically exhausted by the strain of the long, drawn out trial of his personal tax case in Washington, which preceded the trial of the case at bar; and the failure to produce Dobkin was explained on the ground that he was also involved in a tax dispute with the Government and deemed it incompatible with his own interests to appear at the time as an expert witness on behalf of the taxpayer. We think that this contention is without merit. No application was made by the taxpayer for a continuance of the pending case before or during the trial and no claim is made that there were no other witnesses who could testify either as to the facts of the business or as to the useful life of the machines. It is obvious that the Tax Court was guilty of no abuse of discretion in dismissing the motions.

Affirmed.

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 524

AUTOMATIC CIGARETTE SALES CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum findings of fact and opinion of the Tax Court (R. 19–30)[1] are not reported. The opinion of the Court of Appeals (Pet. App. 1–6) is reported at 234 F. 2d 825.

JURISDICTION

The judgment of the Court of Appeals was entered on June 5, 1956. (Pet. App. 1.) By order of Mr. Justice Black on August 21, 1956, the time for filing a petition for a writ of certiorari was extended to October 26, 1956, and the petition was filed on October

[1] Record citations are to the Appendix printed with petitioner's brief in the Court of Appeals. Supplemental record citations are to the Appendix to the respondent's brief in the Court of Appeals, printed separately.

24, 1956. The jurisdiction of this Court is invoked under 28 U. S. C. 1254.

QUESTION PRESENTED

Whether the court below erred in affirming the Tax Court's determination that the entire amount received by petitioner from the operation of gambling machines owned by it and leased to others, including the amount it used to pay fines imposed for unlawfully maintaining the machines, was received by petitioner on its own behalf and not on behalf of the lessees, and was therefore includible in petitioner's gross income under Section 22 (a) of the Internal Revenue Code of 1939.

STATUTE INVOLVED

Internal Revenue Code of 1939:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *
>
> (26 U. S. C. 1952 ed., Sec. 22.)

STATEMENT

The facts, as found by the Tax Court (R. 20–22), are, so far as pertinent to the issue here, as follows:

Petitioner, a West Virginia corporation, was engaged in the year 1944 in the business of buying, selling, and operating coin vending machines, including cigarette, juke box, game and slot machines, and other vending machines. Prior to and during the year 1944, the petitioner owned a substantial number of slot machines. In 1944 it installed a large number of such machines in various locations in the City of Wheeling which were kept and exhibited for gaming purposes in violation both of State law and of an ordinance of that city. (R. 20.)

At that time the city authorities had a policy of imposing a fine on each machine found to be operating in violation of the ordinance. In 1944 the fine imposed was $100, plus costs of $6, assessed and collected in January, June and September. The city manager instructed the chief of police to check periodically and ascertain the number of slot machines in operation. Upon completing the check a list containing the names, addresses, and number of machines found in the various locations, was presented to the judge of the police court, who imposed the fine and costs on each machine. The petitioner was notified of the number of its machines located by the police and made payment of the amount imposed to the proper city authorities. The location pro-

prietor was not served with any warrant nor required to appear before the court. (R. 20–21.)

It was the custom of the petitioner to send two of its agents to the respective locations once a week or more often to collect the proceeds of the machines. The petitioner owned the machines, held the keys, put the machines in operation, serviced, and repaired them. The two collectors attended the opening of the machines in the location proprietor's presence and determined the total proceeds, which were divided on a fifty-fifty basis except that the collectors retained an amount from what would have been the proprietor's share to be applied to the payment of fines and costs. A record was made of the total proceeds, the "proprietor's share", and the amount deducted and retained for the fines. A copy of the receipt was given to the proprietor. A receipt was retained by each collector which was turned over to petitioner's bookkeeper together with the cash proceeds collected. In the case of one location proprietor, the record shows that the fines and costs were deducted prior to the fifty-fifty division of the proceeds of the machines operated in his establishment. (R. 21.)

The petitioner kept no record of the accounts with the specific location proprietors. It maintained an account designated No. 209, bearing the caption "Licenses and Fines Collected and Paid". This account for the taxable year 1944 disclosed that the petitioner had had certain cash receipts and that it paid to the City of Wheeling, by checks on various dates during 1944, sums aggregating $73,246, which is the amount in issue here. Petitioner, in lieu of crediting income

for that amount, credited account No. 209, but these credits had no supporting detail to identify them as the collection of fines from specific establishments. The petitioner did not include the amount of $73,246 in its gross receipts on its income tax return for 1944. (R. 21–22.)

The Tax Court held that the petitioner's gross income should be increased by the amount of $73,246. (R. 27.) The Tax Court denied the petitioner's motion to vacate its decision and reopen the case for taking additional evidence. (R. 36.) The Court of Appeals affirmed the Tax Court's decision. (Pet. App. 1–6.)

ARGUMENT

This case presents a question of fact, namely, whether the amount in controversy was received and used by petitioner on its own behalf, so as to be includible in its gross income. Both courts below sustained the Commissioner's determination which is supported by the evidence. There is no conflict, and no occasion for further review.

The sole issue in this case is whether the funds retained by petitioner to pay the fines regularly imposed by the City of Wheeling were held by petitioner as agent of the individual proprietors of the locations where the machines were placed to meet obligations imposed upon them individually, or whether these funds were retained by petitioner as part of the proceeds of its business to meet an obligation which the city imposed upon petitioner. Petitioner here points to the findings below that in most cases the money for the fines was deducted from what

would otherwise have been the share of the location proprietors. It also points out that the fines were nominally imposed upon the individual location owners. Petitioner argues that the funds must therefore have been held in a fiduciary capacity.

But there was other evidence. The Tax Court found that despite the form of imposing the fines upon the individual proprietors the city looked to petitioner to pay the total fine, and it was petitioner that paid it. The individual proprietors were not served nor required to appear before the court, but on the contrary the city notified petitioner of the amount imposed. Further, petitioner kept no records indicating that it held particular amounts for the account of the various establishments.

On these facts, and the other evidence presented, two courts below found that the amount in controversy represented proceeds of the business retained by petitioner to meet an obligation imposed upon it, and were therefore includible in gross income. This factual conclusion is correct and does not merit review by this Court.

Even on petitioner's assumption that the money which it collected and used to pay the fines came out of the shop proprietors' share of the proceeds, the critical fact remains that the money was used to discharge a legal obligation imposed on petitioner. As the police chief testified (Supp. R. 11), and the courts below pointed out (R. 24–25; Pet. App. 2–3), the city looked only to the owner of the machines (petitioner) for payment of the fines. The money

having been used to discharge petitioner's indebtedness, it represented taxable income to petitioner. Cf. *Old Colony Trust Co.* v. *Commissioner,* 279 U. S. 716.

Other issues, suggested by petitioner, are not raised in this case. They assume, contrary to the findings below, that the funds were held in a fiduciary capacity. Were that the finding, the Government would not contend that they represented income to petitioner.

On the facts as found by the courts below, there is no conflict with decision of this Court or of other courts of appeals.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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NOVEMBER 1956.

U. S. GOVERNMENT PRINTING OFFICE: 1956